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C O R R E C T E D C O P Y -- CORRECTING TEXT

SENSITIVE  
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TREASURY FOR CHRIS BURDICK

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SUBJECT: NORTH CYPRUS BUDGET WOES AND MONEY LAUNDERING  
ISSUES

REF: NICOSIA 363

¶1. (SBU) Summary: The north Cyprus economy continues to deteriorate and the "government" is faced with a relatively massive budget deficit. They are trying to reduce the largest single government expense item, civil servant compensation, but the unions have already begun work-to-rule and strikes which will only get worse after the summer. With all these problems, getting the "government" to focus on a key USG concern, implementation of recently-passed legislation regulating casinos to limit money laundering, will need coordinated pressure from ourselves, the UK and the EU. End Summary.

¶2. (SBU) In an August 3 meeting with the Charge', Turkish Cypriot "Finance Minister," Ersin Tatar, said his government faces a budget deficit of YTL 700 million (US\$ 475 million or 27 percent of the total budget) through December, the "government's" fiscal year end. In return for an emergency injection of YTL 300 million from Turkey, Tatar has pledged to cut his "government's" personnel expenses by YTL 200 million. This is to be accomplished through reductions in overtime pay and adjusting cost of living allowances (COLA) for government workers and pensioners every six months instead of every two months. Once the TC cost-cutting is achieved, Tatar expects to fund the remainder of the deficit through another contribution from Turkey. He justified the Turkish contributions by noting that northern Cyprus "imports almost US\$1.5 billion from Turkey every year and provides free schooling and health care to the thousands of Turkish citizens who live in Cyprus." Note: These residents presumably pay taxes in northern Cyprus like all other residents. End Note.

¶3. (SBU) Tatar claims that many "government" employees double their base pay through overtime earnings in what is already a vastly overstaffed bureaucracy. When asked if he expected civil servant unions to react badly to these measures, Tatar replied "they're a bunch of leftists anyway, they don't vote for us." The civil servant labor unions have already begun to react to these reductions. "Customs" employees have refused to work overtime, and since there is only one shift for work (0700-1400,) all flights and ships that arrive after 1400 are now met only by the police with no customs inspectors present. Policemen are permitted to inspect luggage, but have no authority to confiscate legal goods or assess duties. Press reports suggest that inspections of luggage is not taking place at all after 2 p.m. There reportedly is a boom in sales at the IKEA located on the Greek Cypriot side as TCs load their cars with goods that they now take with them back into the north duty-free (ordinarily, TCs pay duty on imported goods above Euros 265 value.) Other unions,

especially the powerful teachers unions, are reportedly planning to strike against the change in COLA when schools reopen in September.

¶4. (SBU) "Finance Ministry Undersecretary," Zeren Mungan, told us that he expects overtime payment reductions will result in a savings of only YTL 8 million/year while the change in COLA, given the current low inflation levels, will save only YTL 40 million. When asked where the other YTL 152 million in planned savings will be found, Mungan said, clearly indicating his lack of faith in the political leadership, "other unspecified and unknown measures." The problem, according to Mungan, is that both politicians and unions are ultimately confident that, at the end of the day, Turkey will come through with whatever funds are needed.

¶5. (SBU) On August 7, "Economy Minister," Sunat Atun also lamented the state of the TC economy and a sense of helplessness about how to manage the problem. In contrast to his high energy level at our last meeting on May 29 (reftel,) this time Atun was extremely subdued. We asked how the "economic action plan" he had told us his ministry was preparing was proceeding. Atun replied that it has not proceeded at all "because we have no data, no statistics." "All I know," he concluded, "is the economy is a mess and the government must depend on Turkey for its budget."

#### Casino Law and Money Laundering

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¶6. (SBU) We pressed both Tatar and Atun regarding the implementation of laws passed in February 2009 to better regulate casinos to help limit their use as a means to launder money. A regulatory board should have been constituted and a compliance officer named at each casino. So

far, this has not been done despite previous promises by the "ministers" to do so. Mungan explained that, with all the other issues facing the government, "money laundering has simply not been a priority despite good intentions." We told Tatar that if this situation persists, the Financial Action Task Force (FATF), which removed north Cyprus from their watchlist earlier this year in part due to the passage of the casino law, will have no option but to again relegate the jurisdiction to the watchlist. The UK High Commission and the EU Assistance Office plan to join us in lobbying on this issue and they are looking for funds to train compliance officers once a regulatory board is seated.

#### Comment

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¶7. (SBU) Even though GDP continues to decline - estimates are for negative growth of 2-4% this year - the budget and infrastructure fund transfers from Turkey and the high proportion of TCs who receive salaries or pensions from the "government" keep things from getting desperate. The long term damage to the productivity and competitiveness of the private sector, however, will make reintegrating the economies of the north and south of the island more difficult in case of reunification. The lack of progress on implementing the legislation designed to help close off casinos as a means to launder funds is due to a lack of focus by "ministers" overwhelmed with other issues, a lack of understanding of the steps needed to implement the legislation and, we believe, because of the political clout wielded by the casino owners. We plan to work with like-minded embassies and TC bankers to press hard on this matter.

Cohen